EXHIBIT A

COST ACCOUNTING

A Managerial Emphasis

14TH EDITION

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Cost Accounting

A Managerial Emphasis

Fourteenth Edition

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1 The Manager and Management Accounting

Learning Objectives

1. Distinguish financial accounting from management accounting
2. Understand how management accountants affect strategic decisions
3. Describe the set of business functions in the value chain and identify the dimensions of performance that customers are expecting of companies
4. Explain the five-step decision-making process and its role in management accounting
5. Describe three guidelines management accountants follow in supporting managers
6. Understand how management accounting fits into an organization's structure
7. Understand what professional ethics mean to management accountants

All businesses are concerned about revenues and costs.

Whether their products are automobiles, fast food, or the latest designer fashions, managers must understand how revenues and costs behave or risk losing control. Managers use cost accounting information to make decisions related to strategy formulation, research and development, budgeting, production planning, and pricing, among others. Sometimes these decisions involve tradeoffs. The following article shows how companies like Apple make those tradeoffs to increase their profits.

iTunes Variable Pricing: Downloads Are Down, but Profits Are Up[1]

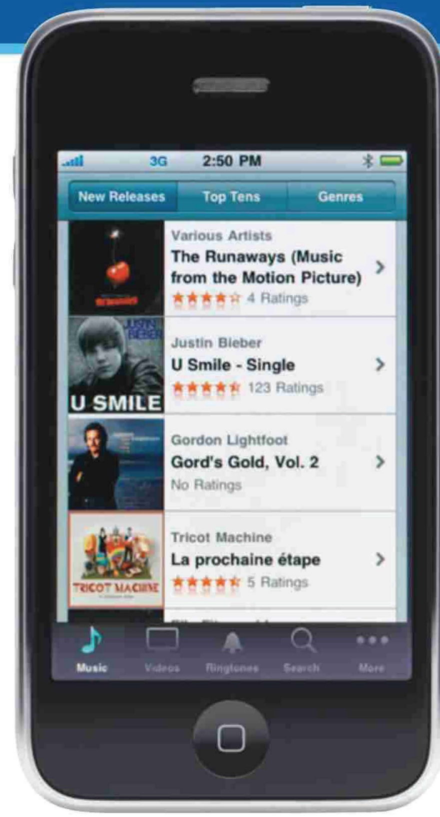
Can selling less of something be more profitable than selling more of it? In 2009, Apple changed the pricing structure for songs sold through iTunes from a flat fee of $0.99 to a three-tier price point system of $0.69, $0.99, and $1.29. The top 200 songs in any given week make up more than one-sixth of digital music sales. Apple now charges the higher price of $1.29 for these hit songs by artists like Taylor Swift and the Black Eyed Peas.

After the first six months of the new pricing model in the iTunes store, downloads of the top 200 tracks were down by about 6%.While the number of downloads dropped, the higher prices generated more revenue than before the new pricing structure was in place. Since Apple's iTunes costs—wholesale song costs, network and transaction fees, and other operating costs—do not vary based on the price of each download, the profits from the 30% increase in price more than made up for the losses from the 6% decrease in volume.

To increase profits beyond those created by higher prices, Apple also began to manage iTunes' costs. Transaction costs (what Apple pays credit-card processors like Visa and MasterCard) have decreased, and Apple has also reduced the number of people working in the iTunes store.

[1] *Sources:* Bruno, Anthony and Glenn Peoples. 2009. Variable iTunes pricing a moneymaker for artists. *Reuters*, June 21. http://www.reuters.com/article/idUSTRE55K0DJ20090621; Peoples, Glenn. 2009. The long tale? *Billboard*, November 14. http://www.billboard.biz/bbbiz/content_display/magazine/features/e3i35ed869fbd929ccdcca52ed7fd9262d3?imw=Y; Savitz, Eric. 2007. Apple: Turns out, iTunes makes money Pacific Crest says; subscription services seems inevitable. *Barron's* "Tech Trader Daily" blog, April 23. http://blogs.barrons.com/techtraderdaily/2007/04/23/apple-turns-out-itunes-makes-money-pacific-crest-says-subscription-service-seems-inevitable/

The study of modern cost accounting yields insights into how managers and accountants can contribute to successfully running their businesses. It also prepares them for leadership roles. Many large companies, such as Constellation Energy, Jones Soda, Nike, and the Pittsburgh Steelers, have senior executives with accounting backgrounds.



Financial Accounting, Management Accounting, and Cost Accounting

As many of you have already seen in your financial accounting class, accounting systems take economic events and transactions, such as sales and materials purchases, and process the data into information helpful to managers, sales representatives, production supervisors, and others. Processing any economic transaction means collecting, categorizing, summarizing, and analyzing. For example, costs are collected by category, such as materials, labor, and shipping. These costs are then summarized to determine total costs by month, quarter, or year. The results are analyzed to evaluate, say, how costs have changed relative to revenues from one period to the next. Accounting systems provide the information found in the income statement, the balance sheet, the statement of cash flow, and in performance reports, such as the cost of serving customers or running an advertising campaign. Managers use accounting information to administer the activities, businesses, or functional areas they oversee and to coordinate those activities, businesses, or functions within the framework of the organization. Understanding this information is essential for managers to do their jobs.

Learning Objective 1

Distinguish financial accounting

. . . . reporting on past performance to external users

from management accounting

. . . helping managers make decisions

Individual managers often require the information in an accounting system to be presented or reported differently. Consider, for example, sales order information. A sales manager may be interested in the total dollar amount of sales to determine the commissions to be paid. A distribution manager may be interested in the sales order quantities by geographic region and by customer-requested delivery dates to ensure timely deliveries. A manufacturing manager may be interested in the quantities of various products and their desired delivery dates, so that he or she can develop an effective production schedule. To simultaneously serve the needs of all three managers, companies create a database—sometimes called a data warehouse or infobarn—consisting of small, detailed bits of information that can be used for multiple purposes. For instance, the sales order database will contain detailed information about product, quantity ordered, selling price, and delivery details (place and date) for each sales order. The database stores information in a way that allows different managers to access the information they need. Many companies are building their own Enterprise Resource Planning (ERP) systems, single databases that collect data and feed it into applications that support the company's business activities, such as purchasing, production, distribution, and sales.

Financial accounting and management accounting have different goals. As many of you know, **financial accounting** focuses on reporting to external parties such as investors, government agencies, banks, and suppliers. It measures and records business transactions and provides financial statements that are based on generally accepted accounting principles (GAAP). The most important way that financial accounting information affects managers' decisions and actions is through compensation, which is often, in part, based on numbers in financial statements.

Management accounting measures, analyzes, and reports financial and nonfinancial information that helps managers make decisions to fulfill the goals of an organization. Managers use management accounting information to develop, communicate, and implement strategy. They also use management accounting information to coordinate product design, production, and marketing decisions and to evaluate performance. Management accounting information and reports do not have to follow set principles or rules. The key questions are always (1) how will this information help managers do their jobs better, and (2) do the benefits of producing this information exceed the costs?

Exhibit 1-1 summarizes the major differences between management accounting and financial accounting. Note, however, that reports such as balance sheets, income statements, and statements of cash flows are common to both management accounting and financial accounting.

Cost accounting provides information for management accounting and financial accounting. **Cost accounting** measures, analyzes, and reports financial and nonfinancial information relating to the costs of acquiring or using resources in an organization. For example, calculating the cost of a product is a cost accounting function that answers financial accounting's inventory-valuation needs and management accounting's decision-making needs (such as deciding how to price products and choosing which products to promote). Modern cost accounting takes the perspective that collecting cost information is a function of the management decisions being made. Thus, the distinction between management accounting and cost accounting is not so clear-cut, and we often use these terms interchangeably in the book.

Decision Point

How is management accounting different from financial accounting?

We frequently hear business people use the term *cost management*. Unfortunately, that term has no uniform definition. We use **cost management** to describe the approaches and activities of managers to use resources to increase value to customers and to achieve organizational goals. Cost management decisions include decisions such as whether to enter new markets, implement new organizational processes, and change product designs. Information from accounting systems helps managers to manage costs, but the information and the accounting systems themselves are not cost management.

Cost management has a broad focus and is not only about reduction in costs. Cost management includes decisions to incur additional costs, for example to improve

Exhibit 1-1 Major Differences Between Management and Financial Accounting

	Management Accounting	Financial Accounting
Purpose of information	Help managers make decisions to fulfill an organization's goals	Communicate organization's financial position to investors, banks, regulators, and other outside parties
Primary users	Managers of the organization	External users such as investors, banks, regulators, and suppliers
Focus and emphasis	Future-oriented (budget for 2011 prepared in 2010)	Past-oriented (reports on 2010 performance prepared in 2011)
Rules of measurement and reporting	Internal measures and reports do not have to follow GAAP but are based on cost-benefit analysis	Financial statements must be prepared in accordance with GAAP and be certified by external, independent auditors
Time span and type of reports	Varies from hourly information to 15 to 20 years, with financial and nonfinancial reports on products, departments, territories, and strategies	Annual and quarterly financial reports, primarily on the company as a whole
Behavioral implications	Designed to influence the behavior of managers and other employees	Primarily reports economic events but also influences behavior because manager's compensation is often based on reported financial results